

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type: <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name: <u>City of Belleville, Michigan</u>	County Wayne
Audit Date June 30, 2004	Opinion Date January 20, 2005	Date Accountant Report Submitted To State: March 16, 2005	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations.

You must check the applicable box for each item below:

- | | |
|---|---|
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| <input checked="" type="checkbox"/> yes <input type="checkbox"/> no | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| <input checked="" type="checkbox"/> yes <input type="checkbox"/> no | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91] or P.A. 55 of 1982, as amended [MCL 38.1132]) |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| <input type="checkbox"/> yes <input checked="" type="checkbox"/> no | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Reports on individual federal assistance programs (program audits).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Single Audit Reports (ASLGU).	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>

Certified Public Accountant (Firm Name): PLANTE & MORAN, PLLC			
Street Address 350 S. Main St., Suite 200	City Ann Arbor	State MI	ZIP 48104
Accountant Signature <i>Plante & Moran, PLLC</i>			

City of Belleville, Michigan

**Financial Statement
with Supplemental Information
June 30, 2004**

City of Belleville, Michigan

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Independent Auditor's Report

To the Honorable Mayor and
Members of the City Council
City of Belleville, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Belleville, Michigan as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Belleville, Michigan's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Belleville, Michigan as of June 30, 2004 and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the budgetary comparison schedules, as identified in the table of contents, are not a required part of the basic financial statements but are supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplemental information. However, we did not audit the information and express no opinion on it.

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To the Honorable Mayor and
Members of the City Council
City of Belleville, Michigan

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Belleville, Michigan's basic financial statements. The accompanying other supplemental information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements. The other supplemental information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

As described in Note 13, the City has implemented a new financial reporting model, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and related statements, as of July 1, 2003.

Plante & Moran, PLLC

January 20, 2005

City of Belleville, Michigan

Management's Discussion and Analysis

Our discussion and analysis of the City of Belleville, Michigan's (the "City") financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2004. Please read it in conjunction with the City's financial statements.

Financial Highlights

As discussed in further detail in this discussion and analysis, the following represents the most significant financial highlights for the year ended June 30, 2004:

- State-shared revenue, our second largest revenue source, was reduced by the State of Michigan by approximately \$45,000 this year. Increases in property tax revenue, federal revenue sources, charges for services, and a special assessment were able to offset this loss, resulting in an increase in fund balance of approximately \$131,000.
- Total net assets related to the City's governmental activities increased by approximately \$58,000, whereas business-type activities increased by approximately \$21,000.
- The City began a long-term investment in its sidewalk infrastructure. Costs associated with phase II of the City's sidewalk project will be funded by a \$79,000 special assessment.

Using this Annual Report

This annual report consists of a series of financial statements. The statement of net assets and the statement of activities provide information about the activities of the City as a whole and present a longer-term view of the City's finances. This longer-term view uses the accrual basis of accounting so that it can measure the cost of providing services during the current year, and whether the taxpayers have funded the full cost of providing government services.

The fund financial statements present a short-term view; they tell us how the taxpayers' resources were spent during the year, as well as how much is available for future spending. Fund financial statements also report the City's operations in more detail than the government-wide financial statements by providing information about the City's most significant funds. The Fiduciary Fund statement provides financial information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

City of Belleville, Michigan

Management's Discussion and Analysis (Continued)

The City as a Whole

The following table shows, in a condensed format, the net assets as of June 30, 2004 (in thousands of dollars):

TABLE I

	Governmental Activities	Business-type Activities	Total
Assets			
Current assets	\$ 1,027	\$ 445	\$ 1,472
Noncurrent assets	2,135	4,434	6,569
Total assets	3,162	4,879	8,041
Liabilities			
Current liabilities	354	258	612
Long-term liabilities	739	2,562	3,301
Total liabilities	1,093	2,820	3,913
Net Assets			
Invested in capital assets -			
Net of related debt	1,511	1,233	2,744
Restricted	136	639	775
Unrestricted	422	187	609
Total net assets	<u>\$ 2,069</u>	<u>\$ 2,059</u>	<u>\$ 4,128</u>

The City's combined net assets increased approximately 1 percent from a year ago - increasing from approximately \$4,048,000 to \$4,128,000. As we look at the governmental activities separately from the business-type activities, we can see that net assets increased approximately \$58,000, or 3 percent.

The current level of unrestricted net assets for our governmental activities stands at \$421,939, or about 16 percent of expenditures. This is within the targeted range set by the City during its last budget process. However, if state-shared revenue continues to trend downward, the City will need to review budgeted expenditure levels. This may include postponing certain projects to ensure this level is maintained without drastically reducing the current level of services provided to the City's residents.

The above table in condensed format is required to be shown in comparative format in fiscal year 2005.

City of Belleville, Michigan

Management's Discussion and Analysis (Continued)

The following table shows the changes of the net assets during the current year (in thousands of dollars):

TABLE 2

	Governmental Activities	Business-type Activities	Total
Revenue			
Program revenue:			
Charges for services	\$ 581	\$ 792	\$ 1,373
Operating grants and contributions	576	-	576
Capital grants and contributions	-	14	14
General revenue:			
Property taxes	1,094	-	1,094
State-shared revenue	401	-	401
Unrestricted investment earnings	27	38	65
Franchise fees	54	-	54
Miscellaneous	15	136	151
Total revenue	2,748	980	3,728
Program Expenses			
General government	410	-	410
Public safety	1,336	-	1,336
Public works	541	-	541
Health and welfare	168	-	168
Recreation and culture	224	-	224
Interest on long-term debt	10	-	10
Water and sewer	-	960	960
Total program expenses	2,689	960	3,649
Change in Net Assets	\$ 59	\$ 20	\$ 79

The above table in condensed format is required to be shown in comparative format in fiscal year 2005.

City of Belleville, Michigan

Management's Discussion and Analysis (Continued)

Governmental Activities

The City's total governmental revenues net of current year expenses resulted in an increase of approximately \$58,000 in net assets, despite decreases in state-shared revenue and interest income. The increase was primarily due to the continuing increase in property tax revenue, charges for services, and federal grants. Also, the City set in motion phase II of a sidewalk project that resulted in a special assessment of approximately \$79,000.

An uptick in expenditures was led by increases in health care costs, police and fire salaries, and property insurance rates. To offset this, the City closely monitored its spending in all other areas including foregoing projects that did not have an imminent need.

Business-type Activities

The City's business-type activities consist of the Water and Sewer Fund. We provide water to residents from the Detroit Water System. We provide sewage treatment through the Downriver Sewage Treatment System. The City is participating in a consent decree with other surrounding communities including Wayne County to expand this system and eliminate any violations of the Clean Water Act. The total estimated cost of this project to the City is approximately \$2,323,000, of which \$465,000 has been funded through water and sewer rates.

In 2004, it was a wetter-than-average year, which resulted in relatively less usage in the water system. In addition, the City's water loss was higher than years past due to water main breaks. The City was able to mitigate these factors by controlling operating and administrative costs. These combined factors resulted in operating income of approximately \$133,000 in the current year.

The City's Funds

Our analysis of the City's major funds begins on page 11, following the government-wide financial statements. The fund financial statements provide detail information about the most significant funds, not the City as a whole. The City Council creates funds to help manage money for specific purposes as well as to show accountability for certain activities. The City's major funds for 2004 include the General Fund and the Major Streets Fund.

The General Fund pays for most of the City's governmental services. The most significant is public safety, which incurred expenses of approximately \$1,211,000, or 54 percent, of the General Fund's total expenditures in 2004. The public safety department is funded primarily by the City's operating millage. This same millage funds other significant activities of the General Fund, including recreation and culture and public works.

City of Belleville, Michigan

Management's Discussion and Analysis (Continued)

General Fund Budgetary Highlights

Over the course of the year, the City amended the budget to take into account events during the year. The most significant change was to increase the estimated transfer from other funds by approximately \$94,000 to help fund increases in public work expenditures for the year. City departments, besides the public works department, overall stayed below budget, resulting in total expenditures approximately \$130,000 above budget. Increases in federal sources and special assessments helped mitigate this increase in expenditures, resulting in a modest improvement in the City's fund deficit by approximately \$131,000.

Capital Asset and Debt Administration

At the end of 2004, the City had approximately \$5,930,650 invested in a broad range of capital assets, including buildings, police and fire equipment, and water and sewer lines. In addition, the City has invested significantly in roads within the City. The City is also participating in a construction project with other surrounding communities including Wayne County to expand the capacity of the downriver sewage treatment system. The estimated cost of this project is approximately \$2,323,000.

Economic Factors and Next Year's Budgets and Rates

The City's budget for next year calls for a freeze on property tax rates. This can be accomplished because of continued growth in our tax base. Because of the impact of Proposal A, however, the City needs to continue to watch its budget very closely. The state-wide Tax Reform Act limits growth in taxable value on any individual property to the lesser of inflation or 5 percent. Because some properties increase in value by less than inflation, the mathematical result of this is that the total taxable value for the City will grow less than by inflation, before considering new property additions.

We anticipate water and sewer rates will remain constant in 2005. The City continually monitors the adequacy of the rate compared to operating costs. Any increase in operating costs, including cost of purchasing water from the City of Detroit, may result in future increases in the City's water and sewer rate. Any proposed increase will likely involve a public hearing to discuss the need for such an increase.

Contacting the City's Management

This financial report is intended to provide our citizens, taxpayers, customers, and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional information, we welcome you to contact the clerk's office.

City of Belleville, Michigan

Statement of Net Assets June 30, 2004

	Primary Government			Component Unit
	Governmental	Business-type		Downtown
	Activities	Activities	Total	Development
				Authority
Assets				
Cash and investments (Note 3)	\$ 649,118	\$ 274,155	\$ 923,273	\$ 473,933
Receivables - Net:				
Customers	-	161,177	161,177	-
Special assessment	48,400	26,939	75,339	-
Other	25,478	1,894	27,372	-
Due from other governmental units	282,888	-	282,888	-
Due from primary government	-	-	-	333,140
Internal balances	18,804	(18,804)	-	-
Note receivable	-	-	-	43,334
Prepaid costs and other assets	1,939	-	1,939	-
Restricted assets (Note 1)	-	638,682	638,682	-
Capital assets - Net (Note 4)	2,135,516	3,795,134	5,930,650	2,458,362
Total assets	3,162,143	4,879,177	8,041,320	3,308,769
Liabilities				
Accounts payable	62,689	61,287	123,976	39,223
Due to other governmental units	88,916	-	88,916	-
Due to component unit	160,597	172,543	333,140	-
Accrued and other liabilities	17,154	24,593	41,747	26,188
Deferred revenue (Note 6)	25,000	-	25,000	-
Noncurrent liabilities (Note 7):				
Due within one year	93,620	152,953	246,573	180,000
Due in more than one year	542,730	2,409,304	2,952,034	1,950,000
Long-term portion of compensated absences	102,616	-	102,616	-
Total liabilities	1,093,322	2,820,680	3,914,002	2,195,411
Net Assets				
Invested in capital assets - Net of related debt	1,510,568	1,232,877	2,743,445	328,362
Restricted:				
Cemetery perpetual care	23,102	-	23,102	-
Streets and highways	84,000	-	84,000	-
Building department	29,212	-	29,212	-
Debt service	-	638,682	638,682	-
Unrestricted	421,939	186,938	608,877	784,996
Total net assets	\$ 2,068,821	\$ 2,058,497	\$ 4,127,318	\$ 1,113,358

City of Belleville, Michigan

		Program Revenues		
		Charges for	Operating	Capital Grants
	Expenses	Services	Grants and Contributions	and Contributions
Functions/Programs				
Primary government:				
Governmental activities:				
General government	\$ 410,034	\$ 208,600	\$ 170,008	\$ -
Public safety	1,336,352	152,578	142,165	-
Public works	541,490	34,892	263,624	-
Health and welfare	168,010	106,302	-	-
Recreation and culture	223,945	78,246	-	-
Interest on long-term debt	9,750	-	-	-
Total governmental activities	2,689,581	580,618	575,797	-
Business-type activities - Water and sewer	959,909	792,050	-	14,395
Total primary government	<u>\$ 3,649,490</u>	<u>\$ 1,372,668</u>	<u>\$ 575,797</u>	<u>\$ 14,395</u>
Component unit - Downtown Development Authority	<u>\$ 912,034</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
General revenues:				
Property taxes				
State-shared revenues				
Unrestricted investment earnings				
Franchise fees				
Miscellaneous				
Total general revenues				
Change in Net Assets				
Net Assets - Beginning of year				
Net Assets - End of year				

Statement of Activities Year Ended June 30, 2004

Net (Expense) Revenue and Changes in Net Assets			
Primary Government			Component Unit
Governmental Activities	Business-type Activities	Total	
\$ (31,426)	\$ -	\$ (31,426)	\$ -
(1,041,609)	-	(1,041,609)	-
(242,974)	-	(242,974)	-
(61,708)	-	(61,708)	-
(145,699)	-	(145,699)	-
(9,750)	-	(9,750)	-
(1,533,166)	-	(1,533,166)	-
-	(153,464)	(153,464)	-
(1,533,166)	(153,464)	(1,686,630)	-
-	-	-	(912,034)
1,093,683	-	1,093,683	771,859
401,074	-	401,074	-
27,011	38,050	65,061	29,090
54,114	-	54,114	-
15,410	136,216	151,626	1,820
1,591,292	174,266	1,765,558	802,769
58,126	20,802	78,928	(109,265)
2,010,695	2,037,695	4,048,390	1,222,623
\$ 2,068,821	\$ 2,058,497	\$ 4,127,318	\$ 1,113,358

City of Belleville, Michigan

Governmental Funds Balance Sheet June 30, 2004

	General Fund	Major Streets Fund	Other Nonmajor Governmental Funds	Total Governmental Funds
Assets				
Cash and investments	\$ 39,648	\$ 41,779	\$ 567,691	\$ 649,118
Receivables:				
Special assessment	48,400	-	-	48,400
Other	22,749	2,729	-	25,478
Due from other governmental units	209,660	-	-	209,660
Due from other funds	96,014	79,766	60,743	236,523
Prepaid expenses and other assets	1,907	32	-	1,939
	<u>418,378</u>	<u>124,306</u>	<u>628,434</u>	<u>1,171,118</u>
Total assets	\$ 418,378	\$ 124,306	\$ 628,434	\$ 1,171,118
Liabilities and Fund Balances (Deficit)				
Liabilities				
Accounts payable	\$ 44,237	\$ 6,457	\$ 11,995	\$ 62,689
Due to other governmental units	17,154	-	-	17,154
Due to other funds	189,629	13,228	14,862	217,719
Due to component unit	64,181	96,416	-	160,597
Accrued and other liabilities	79,996	3,754	5,166	88,916
Deferred revenue	93,816	-	-	93,816
	<u>489,013</u>	<u>119,855</u>	<u>32,023</u>	<u>640,891</u>
Total liabilities	489,013	119,855	32,023	640,891
Fund Balances (Deficit)				
Reserved for cemetery perpetual care	-	-	203,102	203,102
Unreserved, reported in:				
General Fund	(70,635)	-	-	(70,635)
Special Revenue Funds	-	4,451	369,599	374,050
Capital Projects Fund	-	-	23,710	23,710
	<u>(70,635)</u>	<u>4,451</u>	<u>596,411</u>	<u>530,227</u>
Total fund balances (deficit)	(70,635)	4,451	596,411	530,227
Total liabilities and fund balances (deficit)	\$ 418,378	\$ 124,306	\$ 628,434	\$ 1,171,118
Fund Balance - Total Governmental Funds				\$ 530,227
Amounts reported for governmental activities in the statement of net assets are different because:				
Capital assets used in governmental activities are not financial resources and are not reported in the funds				2,135,516
State revenue-sharing payment received 60 days after year end is not reported in the funds				73,228
Amounts earned during the year but not received within 60 days after year end are not reported in the funds				68,816
Compensated absences are included as a liability in governmental activities				(114,018)
Long-term liabilities are not due and payable in the current period and are not reported in the funds				(624,948)
Net Assets of Governmental Activities				<u>\$ 2,068,821</u>

City of Belleville, Michigan

Governmental Funds Statement of Revenue, Expenditures, and Changes in Fund Balances (Deficit) Year Ended June 30, 2004

	General Fund	Major Streets Fund	Other Nonmajor Governmental Funds	Total Governmental Funds
Revenue				
Property taxes	\$ 1,093,683	\$ -	\$ -	\$ 1,093,683
State sources	558,653	189,720	128,850	877,223
Federal sources	208,144	-	-	208,144
Licenses and permits	831	-	96,233	97,064
Interest and rent	55,387	185	12,936	68,508
Charges for services	271,838	-	77,660	349,498
District Court	52,091	-	-	52,091
Other	123,255	-	10,380	133,635
Total revenue	2,363,882	189,905	326,059	2,879,846
Expenditures				
Current:				
General government	433,621	-	-	433,621
Public safety	1,211,107	-	95,196	1,306,303
Public works	481,691	117,666	45,755	645,112
Recreation and culture	122,262	-	96,962	219,224
Other	-	12,809	12,566	25,375
Capital outlay	-	-	49,305	49,305
Debt service	-	53,083	-	53,083
Total expenditures	2,248,681	183,558	299,784	2,732,023
Excess of Revenue Over Expenditures	115,201	6,347	26,275	147,823
Other Financing Sources (Uses)				
Transfers in	63,296	-	47,305	110,601
Transfers out	(47,305)	-	(63,296)	(110,601)
Total other financing sources (uses)	15,991	-	(15,991)	-
Net Change in Fund Balance	131,192	6,347	10,284	147,823
Fund Balances (Deficit) - Beginning of year	(201,827)	(1,896)	586,127	382,404
Fund Balances (Deficit) - End of year	<u>\$ (70,635)</u>	<u>\$ 4,451</u>	<u>\$ 596,411</u>	<u>\$ 530,227</u>

City of Belleville, Michigan

Governmental Funds Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balances (Deficit) of Governmental Funds to the Statement of Activities Year Ended June 30, 2004

Net Change in Fund Balances - Total Governmental Funds	\$ 147,823
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Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures; in the statement of activities, these costs are allocated over their estimated useful lives as depreciation	(104,681)
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Revenue reported in the statement of activities in a previous year that did not provide current financial resources and is reported as revenue in the governmental funds in the year collected	(131,031)
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Repayment of bond principal is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt)	147,141
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Increase in accumulated employee sick and vacation pay, as well as estimated general liability claims, is recorded when earned in the statement of activities	<u>(1,126)</u>
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Change in Net Assets of Governmental Activities	<u>\$ 58,126</u>
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City of Belleville, Michigan

Proprietary Fund Enterprise Fund - Water and Sewer Fund Statement of Assets June 30, 2004

Assets

Cash and investments	\$ 274,155
Receivables:	
Customers	161,177
Special assessment	26,939
Other	1,894
Due from other funds (Note 5)	<u>43,703</u>
Total current assets	507,868
Noncurrent assets:	
Restricted assets (Note 1)	638,682
Capital assets (Note 4)	<u>3,795,134</u>
Total noncurrent assets	<u>4,433,816</u>
Total assets	4,941,684

Liabilities

Current liabilities:	
Accounts payable	61,287
Due to other funds (Note 5)	62,507
Due to component unit (Note 5)	172,543
Accrued and other liabilities	24,593
Current portion of long-term debt (Note 7)	<u>152,953</u>
Total current liabilities	473,883
Noncurrent liabilities - Long-term debt - Net of current portion (Note 7)	<u>2,409,304</u>
Total liabilities	<u>2,883,187</u>

Net Assets

Investment in capital assets - Net of related debt	1,232,877
Restricted for debt service	638,682
Unrestricted	<u>186,938</u>
Total net assets	<u><u>\$ 2,058,497</u></u>

City of Belleville, Michigan

Proprietary Fund Enterprise Fund - Water and Sewer Fund Statement of Revenue, Expenses, and Changes in Net Assets Year Ended June 30, 2004

Operating Revenue	
Water sales	\$ 375,383
Sewage disposal	375,966
Charges for services	40,701
Other revenue	<u>136,216</u>
Total operating revenue	928,266
Operating Expenses	
Cost of water	191,277
Cost of sewage disposal	188,097
Operations and maintenance	74,249
General and administrative	214,043
Depreciation	<u>127,381</u>
Total operating expenses	<u>795,047</u>
Operating Income	133,219
Nonoperating Revenue (Expense)	
Investment income	38,050
Interest expense	<u>(164,862)</u>
Total nonoperating revenue	<u>(126,812)</u>
Change in Net Assets - Before capital contributions	6,407
Capital Contributions - Contributions of lines	<u>14,395</u>
Change in Net Assets	20,802
Net Assets - Beginning of year	<u>2,037,695</u>
Net Assets - End of year	<u><u>\$ 2,058,497</u></u>

City of Belleville, Michigan

Proprietary Fund Enterprise Fund - Water and Sewer Fund Statement of Cash Flows Year Ended June 30, 2004

Cash Flows from Operating Activities

Receipts from customers	\$ 1,127,131
Payments to suppliers	(480,360)
Payments to employees	<u>(190,586)</u>
Net cash provided by operating activities	456,185

Cash Flows from Capital and Related Financing Activities

Purchase of capital assets	(4,675)
Collection of customer assessments (principal and interest)	8,980
Principal and interest paid on capital debt	(442,248)
Increase in restricted assets held by the County	<u>(85,896)</u>
Net cash used in capital and related financing activities	(523,839)

Cash Flows from Investing Activities - Interest received on investments 38,050

Net Decrease in Cash and Investments (29,604)

Cash and Investments - Beginning of year 782,440

Cash and Investments - End of year \$ 752,836

Balance Sheet Classification of Cash and Investments

Cash and investments	\$ 274,155
Restricted cash (Note 1)	<u>478,681</u>
Total cash and cash equivalents	<u><u>\$ 752,836</u></u>

Reconciliation of Operating Income to Net Cash from Operating Activities

Operating income	\$ 133,219
Adjustments to reconcile operating income to net cash from operating activities:	
Depreciation and amortization	127,381
Changes in assets and liabilities:	
Receivables	20,500
Due from other funds	(26,687)
Accounts payable	(7,445)
Accrued and other liabilities	4,165
Due to other funds	<u>205,052</u>
Net cash provided by operating activities	<u><u>\$ 456,185</u></u>

Noncash Investing, Capital, and Financing Activities - The City has assets held at Wayne County for the purpose of financing the construction of water and sewer lines. During the year ended June 30, 2004, interest income of \$2,877 was earned on these assets. During the year ended June 30, 2004, the Water and Sewer Fund received \$14,395 of lines donated by developers.

City of Belleville, Michigan

Fiduciary Fund Agency Fund Statement of Assets and Liabilities June 30, 2004

Assets

Cash and investments	\$ 52,563
Taxes receivable	<u>28,323</u>

Total assets	<u><u>\$ 80,886</u></u>
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Liabilities

Accounts payable	\$ 11,794
Accrued and other liabilities	37,768
Due to other governmental units	<u>31,324</u>

Total liabilities	<u><u>\$ 80,886</u></u>
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Note I - Summary of Significant Accounting Policies

The accounting policies of the City of Belleville, Michigan (the "City") conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the City of Belleville, Michigan:

Reporting Entity

The City of Belleville, Michigan is governed by an elected five-member council. The accompanying financial statements present the City and its component unit, an entity for which the City is considered to be financially accountable. Although blended component units are legal separate entities, in substance, they are part of the City's operations. Each discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City.

Discretely Presented Component Unit - The Downtown Development Authority (the "Authority") is governed by a nine-member board that is appointed by the City Council. The Authority is reported as if it were part of the primary government because the City Council retains responsibility for the activities, finances, and commitments of the Authority. In addition, the Authority's budget is subject to approval by the City Council. The Downtown Development Authority was created to correct and prevent deterioration in the downtown district, encourage historical preservation, and to promote economic growth within the downtown district.

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component unit. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component unit for which the primary government is financially accountable.

Note 1 - Summary of Significant Accounting Policies (Continued)

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenue.

Separate financial statements are provided for governmental funds, proprietary funds, and the fiduciary fund, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual Enterprise Funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. The following major revenue sources meet the availability criterion: state-shared revenue, district court fines, and interest associated with the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Note 1 - Summary of Significant Accounting Policies (Continued)

The City reports the following major governmental funds:

General Fund - The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

Major Streets Fund - The Major Streets Fund is used to account for the resource of state gas and weight tax revenues that are restricted for use on major roads.

The City reports the following major proprietary fund:

Water and Sewer Fund - The Water and Sewer Fund accounts for the activities of the water distribution system and sewage collection system.

Additionally, the City reports the following fund types:

Agency Fund - The Agency Fund is used to account for assets held by the City in a trustee capacity or as an agent for individuals, organizations, other governments, or other funds. The Agency Fund is custodial in nature (assets equal liabilities) and does not involve the measurement of results of operations.

Private sector standards of accounting issued prior to December 1, 1989 are generally followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with the standards of the Governmental Accounting Standards Board. The City has elected not to follow private sector standards issued after November 30, 1989 for its business-type activities.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City's water and sewer function and various other functions of the City. Eliminations of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenue include: (1) charges to customers or applicants for goods, services, or privileges provided, (2) operating grants and contributions, and (3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all taxes.

Note 1 - Summary of Significant Accounting Policies (Continued)

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering foods in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of our proprietary funds relates to charges to customers for sales and services. The Water and Sewer Fund also recognizes the portion of tap fees intended to recover current costs (e.g., labor and materials to hook up new customers) as operating revenue. The portion intended to recover the cost of the infrastructure is recognized as nonoperating revenue. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

Property Tax Revenue

Property taxes are levied on each July 1 on the taxable valuation of property as of the preceding December 31. Taxes are considered delinquent on March 1 of the following year, at which time penalties and interest are assessed.

The 2003 taxable valuation of the City totaled approximately \$91,169,000 (a portion of which is captured by the DDA), on which ad valorem taxes levied consisted of 16.6 mills for operating purposes. This resulted in approximately \$1,094,000 for operations. These amounts are recognized in the General Fund financial statements as tax revenue.

Assets, Liabilities, and Net Assets or Equity

Bank Deposits and Investments - Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. Investments are stated at fair value based on quoted market prices.

Receivables and Payables - In general, outstanding balances between funds are reported as "due to/from other funds." Activity between funds that is representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as "advances to/from other funds." Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances." All trade and property tax receivables are shown as net of allowance for uncollectible amounts.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 1 - Summary of Significant Accounting Policies (Continued)

Restricted Assets - The revenue bonds of the Enterprise Fund require amounts to be set aside for construction, debt service, operations and maintenance, and a bond reserve. These amounts have been classified as restricted assets, as well as amounts on deposit at the County being held for the construction or debt service of the City of Belleville, Michigan's water and sewer lines.

Restricted assets at June 30, 2004 consist of the following:

County sewage disposal system bonds - Assets held at the County for future debt payments	\$ 160,001
Cash and cash equivalents	<u>478,681</u>
Total restricted assets	<u>\$ 638,682</u>

Capital Assets - Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than \$500 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

Buildings, equipment, and vehicles are depreciated using the straight-line method over the following useful lives:

Infrastructure	20 to 25 years
Water system and equipment	5 to 50 years
Sewage collection system	30 to 40 years
Equipment machinery and vehicles	5 to 20 years
Buildings and building improvements	25 years
Land improvements	20 to 25 years

Note 1 - Summary of Significant Accounting Policies (Continued)

Compensated Absences (Vacation and Sick Leave) - It is the City's policy to permit employees to accumulate earned but unused sick and vacation pay benefits. There is no liability for unpaid accumulated sick leave since the City does not have a policy to pay any amounts when employees separate from service with the City. All vacation pay is accrued when incurred in the government-wide, proprietary, and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds only for employee terminations as of year end.

Long-term Obligations - In the government-wide financial statements and the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses. Issuance costs are reported as debt service expenditures.

Fund Equity - In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from these estimates.

Note 2 - Stewardship, Compliance, and Accountability

Noncompliance with Legal Provisions - The original and amended budgets as adopted by the City were not in compliance with the Uniform Accounting and Budgeting Act (Public Act 2 of 1968, as amended) as the General Fund and Major Streets Fund had budgeted a deficit at the end of the year.

Budgetary Information - The annual budget is prepared by the City management and adopted by the City Council by the first Monday in June; subsequent amendments are approved by the City Council. Unexpended appropriations lapse at year end; encumbrances are not included as expenditures. The amount of encumbrances outstanding at June 30, 2004 has not been calculated. During the current year, the budget was amended in a legally permissible manner.

Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America for the General Fund and all Special Revenue Funds. The budget document presents information by fund, function, department, and line items. The legal level of budgetary control adopted by the governing body is the activity level. A comparison of actual results of operations to the General Fund budget and Major Special Revenue Fund budget as adopted by the City Council is included in the required supplemental information. The adopted budget for the nonmajor Special Revenue Funds can be obtained at City Hall.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 2 - Stewardship, Compliance, and Accountability (Continued)

Excess of Expenditures Over Appropriations in Budgeted Funds - During the year, the City of Belleville, Michigan incurred expenditures that were in excess of the amounts budgeted, as follows:

	<u>Budget</u>	<u>Actual</u>
General Fund:		
General government:		
Clerk	\$ 58,075	\$ 60,729
Outside services	63,800	68,255
Other	-	6,601
Public Works:		
Department of Public Works	79,920	174,971
Block grant	-	145,810
Senior transportation	19,630	23,228
Recreation and cultural - Library	61,375	61,505
Other financing uses - Transfers to other funds	-	47,305
Major Streets Fund:		
Public works	73,590	117,666
Debt service	47,235	53,083

Fund Deficits - For the year ended June 30, 2004, the General Fund and the Cemetery Special Revenue Fund have fund deficits. The City intends to remedy the deficits through property tax collections, recognition of deferred revenue, and transfers from the Budget Stabilization Fund.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 3 - Deposits and Investments

Michigan Compiled Laws, Section 129.91, authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan. To the extent that cash from various funds has been pooled in an investment vehicle, related investment income is allocated to each fund based on relative participation in the pool, except that Agency Funds investment earnings are allocated to the General Fund.

The City's investment policy, adopted in accordance with State law, permits the City to invest in investment pools organized under the Surplus Funds Investment Act of 1982 and under the Investment Company Act of 1940.

The City of Belleville, Michigan's deposits and investment policies are in accordance with statutory authority.

At year end, the deposits and investments were reported in the basic financial statements in the following categories:

	Governmental Activities	Business-type Activities	Fiduciary Funds	Total Primary Government	Component Units
Cash and investments	\$ 649,118	\$ 274,155	\$ 52,563	\$ 975,836	\$ 473,933
Restricted assets	-	478,681	-	478,681	-
Total	<u>\$ 649,118</u>	<u>\$ 752,836</u>	<u>\$ 52,563</u>	<u>\$ 1,454,517</u>	<u>\$ 473,933</u>

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 3 - Deposits and Investments (Continued)

The breakdown between deposits and investments for the City is as follows:

	Primary Government	Component Unit
Bank deposits (checking accounts, savings accounts, and certificates of deposit)	\$ 1,254,157	\$ 473,587
Investments in U.S. government agency bonds	200,000	-
Petty cash or cash on hand	360	346
Total	<u>\$ 1,454,517</u>	<u>\$ 473,933</u>

The bank balance of the City's deposits is approximately \$1,329,000, of which \$597,000 is covered by federal depository insurance. The remainder was uninsured. The City believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the City evaluates each financial institution with which it deposits City funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

The component unit's deposits had a bank balance of approximately \$472,000, of which \$400,000 was covered by federal depository insurance.

Investments are categorized into these three categories of credit risk:

Category 1 - Insured or registered, with securities held by the City or its agent in the City's name

Category 2 - Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the City's name, and

Category 3 - Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent but not in the City's name

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 3 - Deposits and Investments (Continued)

At year end, the City's investment balances were categorized as follows:

	Category			Reported Amount (Fair Value)
	1	2	3	
Primary government - U.S. government securities	\$ -	\$ 200,000	\$ -	\$ 200,000

Note 4 - Capital Assets

Capital asset activity of the City's governmental (and business-type) activities was as follows:

Governmental Activities	Balance July 1, 2003	Reclassifications	Additions	Disposals and Adjustments	Balance June 30, 2004
Capital assets not being depreciated - Land	\$ 159,200	\$ -	\$ -	\$ -	\$ 159,200
Capital assets being depreciated:					
Land improvements	104,374	-	-	-	104,374
Buildings	635,800	-	-	-	635,800
Building improvements	380,009	-	-	-	380,009
Infrastructure	758,215	-	-	-	758,215
Equipment, machinery, and vehicles	999,401	-	40,000	-	1,039,401
Subtotal	2,877,799	-	40,000	-	2,917,799
Accumulated depreciation:					
Land improvements	4,175	-	4,175	-	8,350
Buildings	76,296	-	25,432	-	101,728
Building improvements	34,340	-	15,200	-	49,540
Infrastructure	93,655	-	37,911	-	131,566
Equipment, machinery, and vehicles	588,336	-	61,963	-	650,299
Subtotal	796,802	-	144,681	-	941,483
Net capital assets being depreciated	2,080,997	-	(104,681)	-	1,976,316
Net capital assets	\$ 2,240,197	\$ -	\$ (104,681)	\$ -	\$ 2,135,516

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 4 - Capital Assets (Continued)

Business-type Activities	Balance July 1, 2003	Additions	Disposals and adjustments	Balance June 30, 2004
Capital assets not being depreciated - Land	\$ 7,872	\$ -	\$ -	\$ 7,872
Capital assets being depreciated:				
Water system and equipment	958,746	4,675	-	963,421
Sewage collection system	5,029,679	14,395	-	5,044,074
Equipment and vehicles	126,191	-	-	126,191
Subtotal	6,114,616	19,070	-	6,133,686
Accumulated depreciation:				
Water system and equipment	487,557	33,602	-	521,159
Sewage collection system	1,645,615	81,679	-	1,727,294
Equipment and vehicles	85,871	12,100	-	97,971
Subtotal	2,219,043	127,381	-	2,346,424
Net capital assets being depreciated	3,895,573	(108,311)	-	3,787,262
Net capital assets	<u>\$ 3,903,445</u>	<u>\$ (108,311)</u>	<u>\$ -</u>	<u>\$ 3,795,134</u>

Depreciation expense was charged to programs of the primary government as follows:

Governmental activities:	
General government	\$ 9,718
Public safety	30,051
Public works	94,397
Recreation and culture	<u>10,515</u>
Total governmental activities	<u>\$ 144,681</u>
Business-type activities - Water/Sewer	<u>\$ 127,381</u>

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 4 - Capital Assets (Continued)

Capital asset activity of the Downtown Development Authority was as follows:

Component Unit Activities	Balance July 1, 2003	Reclassifications	Additions	Disposals and Adjustments	Balance June 30, 2004
Capital assets not being depreciated -					
Land	\$ 170,000	\$ -	\$ -	\$ -	\$ 170,000
Capital assets being depreciated:					
Land improvements	2,449,315	-	-	-	2,449,315
Buildings	65,790	-	-	-	65,790
Building improvements	210,000	-	-	-	210,000
Infrastructure	510,499	-	-	-	510,499
Subtotal	3,235,604	-	-	-	3,235,604
Accumulated depreciation:					
Land improvements	718,882	-	106,865	-	825,747
Buildings	-	-	2,595	-	2,595
Building improvements	8,400	-	8,400	-	16,800
Infrastructure	76,575	-	25,525	-	102,100
Subtotal	803,857	-	143,385	-	947,242
Net capital assets being depreciated	2,431,747	-	(143,385)	-	2,288,362
Net capital assets	\$ 2,601,747	\$ -	\$ (143,385)	\$ -	\$ 2,458,362

Depreciation expense was charged to the Downtown Development Authority in the amount of \$143,385.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 5 - Interfund Receivables, Payables, and Transfers

The composition of interfund balances is as follows:

Receivable Fund	Payable Fund	Amount
Due to/from Other Funds		
General Fund	Major Streets Fund	\$ 13,228
General Fund	Water and Sewer Fund	62,308
General Fund	Other governmental funds	20,478
Major Streets Fund	General Fund	79,494
Major Streets Fund	Other governmental funds	272
Water and Sewer Fund	General Fund	43,703
Other governmental funds	General Fund	60,544
Other governmental funds	Water and Sewer Fund	199
Total		<u>\$ 280,226</u>
Due to/from Primary Government and Component Units		
Component unit - Downtown Development Authority	Primary government - General Fund	\$ 64,181
Component unit - Downtown Development Authority	Primary government - Water and Sewer Fund	172,543
Component unit - Downtown Development Authority	Primary government - Major Streets Fund	96,416
Total		<u>\$ 333,140</u>

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 6 - Deferred Revenue

Governmental funds report deferred revenue in connection with receivables for revenue that is not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received but not yet earned. At the end of the current fiscal year, the various components of deferred revenue are as follows:

	Unavailable	Unearned
Special assessments	\$ 45,863	\$ -
Grant reimbursements received greater than 60 days after year end	22,953	-
Grant payments received prior to meeting all eligibility requirements	-	25,000
Total	<u>\$ 68,816</u>	<u>\$ 25,000</u>

Note 7 - Long-term Debt

The City issues bonds to provide for the acquisition and construction of major capital facilities. General obligation bonds are direct obligations and pledge the full faith and credit of the City. County contractual agreements and installment purchase agreements are also general obligations of the government. Revenue bonds involve a pledge of specific income derived from the acquired or constructed assets to pay debt service.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 7 - Long-term Debt (Continued)

Long-term obligation activity can be summarized as follows:

	Interest Rate	Principal Maturity Ranges	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities							
Installment debt obligations:							
Fire Truck							
Amount of issue - \$221,000	4.9%	-	\$ 62,446	\$ -	\$ (62,446)	\$ -	\$ -
Maturing through 2004							
Note payable - Downtown Development Authority							
Amount of issue - \$130,000	4.5%	\$43,334	86,667	-	(43,333)	43,334	43,334
Maturing through 2005							
Land contract							
Amount of issue - \$90,408	9.0%	\$6,528 -					
Maturing through 2007		\$33,478	70,824	-	(8,543)	62,281	9,344
Land contract							
Amount of issue - \$620,000	6.2%	\$26,700 -					
Maturing through 2016		\$55,156	552,152	-	(32,819)	519,333	29,540
Total installment debt obligations			772,089	-	(147,141)	624,948	82,218
Other long-term obligations - Accumulated employee benefits			112,892	1,126	-	114,018	11,402
Total governmental activities			884,981	1,126	(147,141)	738,966	93,620
Business-type Activities							
County contractual obligations - Revenue Bonds:							
Water Supply and Sewer Disposal System, Series 1992A							
Amount of issue - \$550,000	7.1% -	\$30,000 -					
Maturing through 2013	7.3%	\$45,000	370,000	-	(175,000)	195,000	30,000
Water Supply and Sewer Disposal System, Series 1994							
Amount of issue - \$995,000	6.0% -	\$50,000 -					
Maturing through 2011	6.25%	\$100,000	500,000	-	(45,000)	455,000	50,000
Water Supply and Sewer Disposal System, Series 2002							
Amount of issue - \$995,000	3.75% -	\$20,000 -					
Maturing through 2023	5.4%	\$135,000	995,000	-	-	995,000	20,000
General obligation bonds:							
Downriver Sewer System Debt							
15 issues							
Maturing through 2021	various	various	974,643	-	(57,386)	917,257	52,953
Total business-type activities			2,839,643	-	(277,386)	2,562,257	152,953
Total governmental and business-type activities			\$ 3,724,624	\$ 1,126	\$ (424,527)	\$ 3,301,223	\$ 246,573

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 7 - Long-term Debt (Continued)

Component Unit	Interest Rate	Principal Maturity Ranges	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
County contractual obligations - General obligation bonds							
Limited Tax Bond, Series 1994A							
Amount of issue - \$1,075,000	6.3% -	\$50,000 -					
Maturing through 2014	7.1%	\$100,000	\$ 785,000	\$ -	\$ (50,000)	\$ 735,000	\$ 55,000
Limited Tax Bond, Series 1994B							
Amount of issue - \$825,000	7.0% -						
Maturing through 2013	7.25%	\$70,000	700,000	-	(70,000)	630,000	70,000
General obligation debt							
Amount of issue - \$950,000	4.8% -	\$50,000 -					
Maturing through 2014	5.4%	\$100,000	815,000	-	(50,000)	765,000	55,000
Total component unit			\$ 2,300,000	\$ -	\$ (170,000)	\$ 2,130,000	\$ 180,000

Annual debt service requirements to maturity for the above (governmental) bond and note obligations are as follows:

	Governmental Activities			Business-type Activities			Component Unit		
	Principal	Interest	Total	Principal	Interest	Total	Principal	Interest	Total
2005	\$ 82,218	\$ 35,765	\$ 117,983	\$ 152,953	\$ 107,392	\$ 260,345	\$ 180,000	\$ 133,088	\$ 313,088
2006	44,415	33,585	78,000	169,399	99,724	269,123	185,000	121,705	306,705
2007	79,090	29,735	108,825	180,828	91,298	272,126	195,000	109,751	304,751
2008	38,695	24,905	63,600	197,320	82,093	279,413	205,000	97,066	302,066
2009	41,164	22,436	63,600	213,759	72,042	285,801	215,000	83,648	298,648
2010-2014	248,723	69,277	318,000	1,012,463	224,581	1,237,044	1,150,000	193,888	1,343,888
2015-2019	90,643	4,504	95,147	470,761	86,367	557,128	-	-	-
2020-2024	-	-	-	164,774	17,632	182,406	-	-	-
Total	\$ 624,948	\$ 220,207	\$ 845,155	\$ 2,562,257	\$ 781,129	\$ 3,343,386	\$ 2,130,000	\$ 739,146	\$ 2,869,146

In the prior year, the City defeased certain bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust accounts' assets and liabilities for the defeased bonds are not included in the general purpose financial statements. At June 30, 2004, \$925,000 of bonds outstanding is considered defeased.

Note 8 - Risk Management

The City is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The City has purchased commercial insurance for employee injuries and medical benefit claims and participates in the Michigan Municipal Risk Management Authority risk pool (as a state pool member) for claims relating to loss, torts, and errors and omissions. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

The Michigan Municipal Risk Management Authority's State Pool program operates as a common risk-sharing management program for local units of government in Michigan. Member premiums are used to purchase excess insurance coverage and to pay member claims in excess of deductible amounts. A portion of the excess insurance coverage is underwritten by the Authority itself.

Note 9 - Defined Benefit Pension Plan

Plan Description - The City participates in the Michigan Municipal Employees' Retirement System (MMERS), an agent multiple-employer defined benefit pension plan that covers all employees of the City. The system provides retirement, disability, and death benefits to plan members and their beneficiaries. MMERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to MMERS at 1134 Municipal Way, Lansing, Michigan 48917.

Funding Policy - The obligation to contribute to and maintain the MMERS for these employees was established by negotiation with the City's collective bargaining units.

Effective June 1, 2000, the City agreed to institute the F55/20 waiver of the Michigan Employees' Retirement System Plan. Employee contributions are twenty-six one hundredths of one percent (.26 percent) and employer contributions are fifty one hundredths of one percent (.50 percent) of employees' gross earnings.

City of Belleville, Michigan

Notes to Financial Statements June 30, 2004

Note 9 - Defined Benefit Pension Plan (Continued)

Annual Pension Costs - For the year ended June 30, 2004, the City's annual pension cost of \$116,407 for the plan was equal to the required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at December 31, 2002, using an entry age normal actuarial method. Significant actuarial assumptions used include: (a) an 8 percent investment rate of return, (b) projected salary increases of 4.5 percent per year, attributable to inflation, and (c) an additional salary increase of 0 percent to 4.16 percent per year, attributable to seniority/merit. Both (a) and (b) include an inflation component of 4.5 percent. The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility over a four-year period. The unfunded actuarial liability is being amortized as a level percent of payroll on a closed basis. The remaining amortization period is 27 years.

Three-year trend information is as follows:

	Fiscal Year Ended June 30		
	2002	2003	2004
Annual pension costs (APC)	\$ 108,768	\$ 118,068	\$ 116,407
Percentage of APC contributed	100%	100%	100%
Net pension obligation	\$ -	\$ -	\$ -

	Valuation as of December 31		
	2001	2002	2003
Actuarial value of assets	\$ 2,215,229	\$ 2,261,356	\$ 2,517,325
Actuarial accrued liability (entry age)(AAL)	\$ 3,287,330	\$ 3,659,825	\$ 3,776,872
Unfunded AAL (UAAL)	\$ 1,072,101	\$ 1,398,469	\$ 1,259,547
Funded ratio	67.39%	61.79%	66.70%
Covered payroll	\$ 845,236	\$ 845,447	\$ 994,878
UALL as a percentage of covered payroll	126.84%	165.41%	127.00%

Note 10 - Postretirement Benefits

The City provides health care benefits and life insurance policies to certain full-time employees upon retirement in accordance with labor contracts. Currently, two retirees are eligible for each. Expenditures for postemployment benefits are recognized as the insurance premiums become due; during the year, this amounted to approximately \$16,500.

Note 10 - Postretirement Benefits (Continued)

Upcoming Reporting Change

The Governmental Accounting Standards Board (GASB) has recently released Statement No. 45, *Accounting and Reporting by Employers for Postemployment Benefits Other than Pensions*. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree health care, as well as any other postemployment benefits (other than pensions). The new rules will cause the government-wide financial statements to recognize the cost of providing retiree health care coverage over the working life of the employee, rather than at the time the health care premiums are paid. The new pronouncement is effective for the year ending June 30, 2010.

Note 11 - Commitment

The City had been named as a defendant in a lawsuit alleging violations of the Clean Water Act occurring in the downriver sewage treatment system. Several other communities, including Wayne County, were also named as defendants. Under terms of the consent decree, the communities are required to undertake construction projects to expand the capacity of the system and eliminate any violations of the Clean Water Act. The estimated total cost of the project is \$2,323,000. To date, approximately \$465,000 has been collected through water and sewer rates for debt payments.

Note 12 - Joint Ventures

The City of Belleville, Michigan is a member of a joint venture with Van Buren and Sumpter Townships. The purpose is to provide library services to the residents of all participating communities. The participating communities provide annual funding for its operations, and it is the City of Belleville, Michigan's responsibility to account for and remit these funds to Wayne County for services provided. During the current year, the City contributed approximately \$61,500 for its operations. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Complete financial statements for the joint venture can be obtained from the administrative offices at 6 Main Street, Belleville, MI.

Note 12 - Joint Ventures (Continued)

The City of Belleville, Michigan is a member of a joint venture with Sumpter Township. The purpose is to provide centralized communications, detention facilities, and other related operations to the citizens of the communities for public safety, health, and welfare. The participating communities provide annual funding for its operations. During the current year, the City contributed approximately \$140,000 for its operations. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Financial activity is maintained by Sumpter Township. Financial statements for the joint venture can be obtained from the administrative offices at 23480 Sumpter Road, Belleville, MI.

The City of Belleville, Michigan is a member of a joint venture with Van Buren Township. The purpose is to provide museum services to the residents of all participating communities. The participating communities provide annual funding for its operations. During the current year, the City contributed approximately \$27,000 for its operations. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Financial activity is maintained by Van Buren Township. Financial statements for the joint venture can be obtained from the administrative offices at 46425 Tyler Road, Belleville, MI.

The City of Belleville, Michigan is a member of a joint venture with Van Buren Township, Huron Township, Sumpter Township, and the City of Romulus. The purpose is to provide a shared information network to the local law enforcement agencies. The participating communities provide annual funding for its operations. During the current year, the City contributed approximately \$5,000 for its operations. The City is unaware of any circumstances that would cause an additional benefit or burden to the participating governments in the near future. Financial activity is maintained by Van Buren Township. Financial statements for the joint venture can be obtained from the administrative offices at 46425 Tyler Road, Belleville, MI.

Note 13 - Accounting and Reporting Change

In June 1999, the Governmental Accounting Standards Board (GASB) issued Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. The City of Belleville, Michigan has applied the provisions of this statement in the accompanying financial statements (including the notes to the financial statements). The City has elected to implement both the general provisions of the statement and the retroactive reporting of the infrastructure in the current year. Certain significant changes in the statement include the following:

- During the year, as a result of implementing GASB No. 34, the Expendable Trust Fund was reclassified from a Trust Fund to a Special Revenue Fund.
- A management's discussion and analysis (MD&A) section providing an analysis of the City's overall financial position and results of operations
- Financial statements prepared using full accrual accounting for all of the City's activities, including infrastructure (roads, bridges, etc.)
- A change in the fund financial statements to focus on the major funds
- Capital assets in the governmental activities column of the statement of net assets includes infrastructure assets (roads, bridges, etc.) not previously accounted for by the City as well as assets totaling approximately \$2,918,000 that would previously have been reported in the General Fixed Assets Account Group.
- The governmental activities column includes bonds and other long-term obligations totaling \$738,966 previously reported in the General Long-term Debt Account Group.

Required Supplemental Information

City of Belleville, Michigan

Required Supplemental Information Budgetary Comparison Schedule - General Fund Year Ended June 30, 2004

	Original Budget	Amended Budget	Actual	Variance with Amended Budget
Fund Deficit - Beginning of year	\$ (201,827)	\$ (201,827)	\$ (201,827)	\$ -
Revenues				
Property taxes	1,120,800	1,120,800	1,093,683	(27,117)
Federal sources	50,400	50,400	208,144	157,744
State sources	489,330	475,330	558,653	83,323
Licenses and permits	3,525	3,525	831	(2,694)
District Court	29,000	29,000	52,091	23,091
Charges for services	205,000	230,000	271,838	41,838
Interest and rental income	62,000	62,000	55,387	(6,613)
Special assessments	-	-	50,429	50,429
Other	32,000	32,000	72,826	40,826
Total revenues	1,992,055	2,003,055	2,363,882	360,827
Expenditures				
General government:				
City council	25,795	25,795	23,452	2,343
City manager	61,860	61,860	57,771	4,089
Elections	6,900	6,900	4,853	2,047
Clerk	58,075	58,075	60,729	(2,654)
Treasurer	112,775	112,775	104,734	8,041
Municipal Building	90,330	150,330	107,226	43,104
Outside services	63,800	63,800	68,255	(4,455)
Other	-	-	6,601	(6,601)
Total general government	419,535	479,535	433,621	45,914
Public safety:				
Police	1,135,150	1,139,200	1,113,928	25,272
Fire	96,025	118,025	97,179	20,846
Total public safety	1,231,175	1,257,225	1,211,107	46,118
Public works:				
Department of Public Works	79,920	79,920	174,971	(95,051)
Street lighting	19,000	19,000	17,566	1,434
Vehicle operations	9,000	9,000	5,697	3,303
Sanitation	121,370	121,370	114,419	6,951
Block grant	-	-	145,810	(145,810)
Senior transportation	19,630	19,630	23,228	(3,598)
Total public works	248,920	248,920	481,691	(232,771)
Recreation and cultural:				
Parks	39,025	42,025	33,757	8,268
Cultural activities	27,150	27,150	27,000	150
Library	61,375	61,375	61,505	(130)
Total recreation and cultural	127,550	130,550	122,262	8,288

City of Belleville, Michigan

Required Supplemental Information (Continued) Budgetary Comparison Schedule - General Fund Year Ended June 30, 2004

	Original Budget	Amended Budget	Actual	Variance with Amended Budget
Other Financing Sources (Uses)				
Transfers from other funds	\$ 19,210	\$ 113,175	\$ 63,296	\$ (49,879)
Transfers to other funds	-	-	(47,305)	(47,305)
Total other financing sources (uses)	19,210	113,175	15,991	(97,184)
Total charges to appropriations	2,007,970	2,003,055	2,232,690	229,635
Fund Balance (Deficit) - End of year	\$ (217,742)	\$ (201,827)	\$ (70,635)	\$ 131,192

City of Belleville, Michigan

Required Supplemental Information Budgetary Comparison Schedule Major Special Revenue Fund - Major Streets Fund Year Ended June 30, 2004

	Original Budget	Amended Budget	Actual	Variance with Amended Budget
Fund Deficit - Beginning of year	\$ (1,896)	\$ (1,896)	\$ (1,896)	\$ -
Revenues				
State sources	146,000	146,000	189,720	43,720
Interest income	<u>1,000</u>	<u>1,000</u>	<u>185</u>	<u>(815)</u>
Total revenues	147,000	147,000	189,905	42,905
Expenditures				
Public works	73,590	73,590	117,666	(44,076)
Other	12,900	12,900	12,809	91
Contingencies	12,183	10,000	-	10,000
Debt service	<u>47,235</u>	<u>47,235</u>	<u>53,083</u>	<u>(5,848)</u>
Total expenditures	145,908	143,725	183,558	(39,833)
Other Financing Uses - Transfers out	<u>1,092</u>	<u>1,092</u>	<u>-</u>	<u>1,092</u>
Fund Balance (Deficit) - End of year	<u><u>\$ (1,896)</u></u>	<u><u>\$ 287</u></u>	<u><u>\$ 4,451</u></u>	<u><u>\$ 4,164</u></u>

Other Supplemental Information

City of Belleville, Michigan

	Special Revenue Funds						
	Local Streets	Cemetery	Budget Stabilization	911	Building Department	Expendable Trust Fund	Capital Projects
Assets							
Cash and investments	\$ 43,690	\$ 4,379	\$ 249,570	\$ 9	\$ 41,698	\$ 19,312	\$ 5,931
Due from other funds	<u>38,677</u>	<u>-</u>	<u>4,284</u>	<u>-</u>	<u>3</u>	<u>-</u>	<u>17,779</u>
Total assets	<u>\$ 82,367</u>	<u>\$ 4,379</u>	<u>\$ 253,854</u>	<u>\$ 9</u>	<u>\$ 41,701</u>	<u>\$ 19,312</u>	<u>\$ 23,710</u>
Liabilities and Fund Balances (Deficit)							
Liabilities							
Accounts payable	\$ 212	\$ 1,291	\$ -	\$ -	\$ 10,492	\$ -	\$ -
Accrued and other liabilities	870	2,299	-	-	1,997	-	-
Due to other funds	<u>1,736</u>	<u>1,100</u>	<u>12,026</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	2,818	4,690	12,026	-	12,489	-	-
Fund Balances (Deficit)							
Reserved for cemetery perpetual care	-	-	-	-	-	-	-
Unreserved, reported in:							
Special Revenue Funds	79,549	(311)	241,828	9	29,212	19,312	-
Capital Projects Fund	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>23,710</u>
Total fund balances (deficit)	<u>79,549</u>	<u>(311)</u>	<u>241,828</u>	<u>9</u>	<u>29,212</u>	<u>19,312</u>	<u>23,710</u>
Total liabilities and fund balances (deficit)	<u>\$ 82,367</u>	<u>\$ 4,379</u>	<u>\$ 253,854</u>	<u>\$ 9</u>	<u>\$ 41,701</u>	<u>\$ 19,312</u>	<u>\$ 23,710</u>

**Other Supplemental Information
Combining Balance Sheet
Nonmajor Governmental Funds
June 30, 2004**

<u>Permanent</u>	
Cemetery	Total Nonmajor
Perpetual	Governmental
Care	Funds
<u> </u>	<u> </u>
\$ 203,102	\$ 567,691
-	60,743
<u>\$ 203,102</u>	<u>\$ 628,434</u>
\$ -	\$ 11,995
-	5,166
-	14,862
<u> </u>	<u> </u>
-	32,023
203,102	203,102
-	369,599
-	23,710
<u> </u>	<u> </u>
203,102	596,411
<u>\$ 203,102</u>	<u>\$ 628,434</u>

City of Belleville, Michigan

	Special Revenue Funds						
	Local Streets	Cemetery	Budget Stabilization	911	Building Department	Expendable Trust Fund	Capital Projects
Revenue							
State sources	\$ 65,554	\$ -	\$ -	\$ 63,296	\$ -	\$ -	\$ -
Interest	395	815	11,428	-	268	-	30
Charges for services	-	77,660	-	-	-	-	-
Other revenue	-	-	-	-	38	1,992	-
Licenses and permits	-	-	-	-	96,233	-	-
Total revenue	65,949	78,475	11,428	63,296	96,539	1,992	30
Expenditures							
Highways, streets, and bridges	45,755	-	-	-	-	-	-
Parks and community service	-	96,850	-	-	-	-	-
Other	4,299	7,068	-	-	-	1,199	-
Capital outlay	-	-	-	-	-	-	49,305
Building inspection	-	-	-	-	95,196	-	-
Total expenditures	50,054	103,918	-	-	95,196	1,199	49,305
Excess of Revenue Over (Under)							
Expenditures	15,895	(25,443)	11,428	63,296	1,343	793	(49,275)
Other Financing Sources (Uses)							
Operating transfers in	-	-	-	-	-	-	47,305
Operating transfers out	-	-	-	(63,296)	-	-	-
Total other financing sources (uses)	-	-	-	(63,296)	-	-	47,305
Net Change in Fund Balance	15,895	(25,443)	11,428	-	1,343	793	(1,970)
Fund Balances - Beginning of year	63,654	25,132	230,400	9	27,869	18,519	25,680
Fund Balances (Deficit) - End of year	<u>\$ 79,549</u>	<u>\$ (311)</u>	<u>\$ 241,828</u>	<u>\$ 9</u>	<u>\$ 29,212</u>	<u>\$ 19,312</u>	<u>\$ 23,710</u>

Other Supplemental Information
Combining Statement of Revenue, Expenditures, and Changes
in Fund Balances (Deficit) - Nonmajor Governmental Funds
Year Ended June 30, 2004

<u>Permanent</u>	
Cemetery Perpetual Care	Total Nonmajor Governmental Funds
\$ -	\$ 128,850
-	12,936
-	77,660
8,350	10,380
-	96,233
8,350	326,059
-	45,755
112	96,962
-	12,566
-	49,305
-	95,196
112	299,784
8,238	26,275
-	47,305
-	(63,296)
-	(15,991)
8,238	10,284
194,864	586,127
<u>\$ 203,102</u>	<u>\$ 596,411</u>



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January 20, 2005

Honorable Mayor and Members
of the City Council
City of Belleville
6 Main Street
Belleville, MI 48111

Dear Mayor and Council Members:

Dear Council Members:

We recently completed the audit of the financial statements of the City of Belleville for the year ended June 30, 2004. In addition to the audit report, we offer the following comments for your consideration.

REPORTABLE CONDITIONS

In planning and performing our audit of the City's financial statements, we considered the City's internal control structure in order to determine our audit procedures for the purpose of expressing our opinion on the financial statements. The consideration we gave to the internal control structure was not sufficient for us to provide any form of assurance. However, we noted items concerning the internal control structure and operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions are significant deficiencies in the design or operation of the internal control structure that have come to our attention and, in our judgment, could adversely affect the City's ability to record, process, summarize and report financial data consistent with the City's management assertions inherent in the financial statements. We consider the following items to be reportable conditions.

Bank Account Reconciliations

Again this year, the City failed to timely reconcile certain bank accounts. Bank reconciliations are an important control feature for the City that helps prevent and detect material misstatements in the City's general ledger. The lack of timely preparation exasperated accounting errors identified during the audit. Accordingly, we highly recommend someone independent of the collection and recording functions reconcile the bank accounts on a timely basis. Furthermore, someone independent of the bank reconciliation process should review the reconciliation for timeliness, completeness and accuracy.

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Utility Billing Registers

We noticed no formal reconciliation between the customer billing register and the general ledger. Unusual relationships and differences between these two reports may have existed and not been addressed on a timely basis. We recommend the City implement a monthly closing process that incorporates a utility billing register reconciliation with other important month end closing procedures.

Special Assessment Invoices

During the year, the City assessed certain residents for sidewalk repair. The special assessment was invoiced to the tax payers via a letter from the City versus on their tax bills. Since these invoices did not go through the City's accounting system, they were not recorded until after year end. If the City determines that invoices for a special assessment should be sent prior to tax bills, we recommend that management ensure that these transactions are recorded in the general ledger at the invoice date. This control will provide a way to match collections to billings.

Interfunds

We noticed cash received by the City remained in the General Fund for a significant period of time before being transferred to the appropriate Special Revenue Fund. For example, ACT 51 monies were originally recorded in the general fund and not transferred to the Major and Local Street Funds until several months later. Additionally, the accounting records did not reflect the correct interfund payable or receivable between the two funds. We also noticed instances where banking transfers between City accounts did not agree with the accounting records. Accordingly, an inordinate amount of time was spent during the audit engagement reconciling interfund activity with bank reconciliations to reflect revenue in the appropriate funds.

OTHER FINANCIAL MATTERS

Major Street Fund Debt Payment

During the fiscal year ended June 30, 2003, the Downtown Development Authority (DDA) loaned funds to the major street fund. At the time of the loan, a debt payment schedule was established whereby the major street fund is required to make annual debt service payments to the DDA. As of June 30, 2004, two payments have been required; however, none have been made. The final payment is due on June 30, 2005; therefore, the entire principal and accrued interest of \$141,700 will be due on June 30, 2005.

Water Main/Street Repairs

During the year, there were repairs to the roads in connection with water main breaks. The City accounted for repairs to the streets in the major and local street funds and the repairs to the actual water lines in the water and sewer fund. Since these street repairs were due to a water and sewer problem, the City should consider having the water and sewer fund reimburse the street funds for these expenditures.

State Funding Overview

State shared revenue accounts for approximately 17 percent of the City's total General Fund revenue. Because of slower than anticipated growth in the State's sales tax collections (the sole source of revenue sharing payments to local units of government) and the State's budget problems which have resulted in additional appropriation reductions to the revenue sharing line item in the State's budget, revenue sharing payments for the last several years have been lower than anticipated.

Although sales tax revenue would support an increase to total state shared revenue payments, the State's budget situation remains troublesome at best. As you are probably aware, the Governor's budget for the State's 2004/2005 fiscal year contains a provision to not pay counties statutory revenue sharing (the counties' only source of revenue sharing). Instead, the counties will change their property tax levy date for their operating millage from December to July (beginning in 2005). A portion of the additional funds generated from the early property tax levy will be used by the counties over a multiple year period to replace statutory revenue sharing that will not be paid by the State. The plan calls for the return of statutory revenue sharing for the counties when their restricted monies from the early levy run out. A key part to this plan allows the State to hold revenue sharing payments to cities, villages and townships for the State's 2004/2005 fiscal year at prior year levels. This plan was recently approved by the Michigan legislature and signed by the Governor.

It is generally acknowledged that the State's budget woes will continue for several more years. The Governor recently announced that another \$500 million shortfall exists for the State's 2005/2006 fiscal year budget (the State's 2005/2006 fiscal year budget will be introduced by the Governor in early 2005). Also, during October 2004, the Governor announced that her administration might introduce a significant tax restructuring proposal shortly. Specific details of the proposal have not been formally announced and the impact on significant revenue sources to local governments, such as personal property taxes and revenue sharing, is not known. As a result of the continuing uncertainty with the State's budget situation and other potential developments with changes to State's tax structure, we continue to urge the City to be very conservative in its estimation of state shared revenue as this line item in the State's budget remains vulnerable.

The table below details state shared revenue for the City over the past five years broken out by statutory and constitutional portions. In addition, it details the total decrease in state shared revenue experienced by the City compared to the State's fiscal year 2001.

	<u>Actual FY 2001</u>	<u>Actual FY 2002</u>	<u>Actual FY 2003</u>	<u>Estimated FY 2004</u>	<u>Estimated FY 2005</u>
Constitutional	\$ 259,374	\$ 262,016	\$ 266,452	\$ 263,558	\$ 274,801
Statutory	214,960	197,966	176,944	134,945	123,702
Total payments	<u>\$ 474,334</u>	<u>\$ 459,982</u>	<u>\$ 443,396</u>	<u>\$ 398,503</u>	<u>\$ 398,503</u>
Dollar change		\$ (14,352)	\$ (16,586)	\$ (44,893)	\$ -
Percentage change		-3.03%	-3.61%	-10.12%	0.00%

We will continue to update the City as developments occur.

LEGISLATIVE MATTERS

Transportation

The Legislature recently approved HB 5319 which would earmark one-half of one cent of the state gasoline tax for the preservation, improvement or reconstruction of existing bridges. It is estimated that over the next 10 years that approximately a half billion dollars will be available to local governments for bridge needs. Presently, these monies are used primarily by the Michigan Department of Transportation for State bridges. The legislation creates a Local Bridge Authority to manage the monies as well seven, five member, regional bridge councils. The new Authority would consist of six voting members appointed by the State Transportation Commission (three nominations by the County Road Association of Michigan and three by the Michigan Municipal League) and two non-voting members nominated by the Department of Transportation.

Also, HB 4358 has been introduced which changes vehicle weight restrictions on Michigan roads for certain trucks (without regard to existing limitations imposed by local governments) and could reduce overweight truck fines.

Property Tax

During the recent legislative session, there were a number of bills involving property taxes that impact local governments. The following is a highlight of several of the bills:

- HB 4880, as passed by the House in August 2004, proposes to increase property taxes for mobile home owners with additional monies earmarked for local governments.
- HB6017 was introduced to address the inconsistent treatment of assessing commercial property using the occupancy method. The inconsistent treatment occurs when the taxable value of a commercial property is reduced based on a loss in occupancy and a corresponding increase will not occur when occupancy increases resulting in a permanent taxable cap on property (subject to annual inflationary increases). This treatment is a result of what is commonly referred to as the "WPW" Case" involving the City of Troy.
- HB 4649 was passed by the House and would allow local governments to pass a resolution exempting new construction on homestead property used as a living area from property taxes (subject to certain limitations) in all or just certain areas of the local jurisdiction.
- HB 5358 was introduced and would change the requirements for personal property tax examiners including: requiring the State Tax Commission to qualify examiners based on experience and examination; require examiners to be employees of a local government; and make payments to examiners on a per parcel basis.

- HB 5538, as passed by the House, exempts property under development from school operating taxes (18 mills) by classifying the property as “homestead” property. The bill also proposes to not allow the taxable value of property to “uncap” when the property is sold to a new owner.
- HB 4234, as passed by the House, would provide a personal property tax exemption to businesses with taxable value of personal property of \$7,500 or less (these businesses would be exempt from paying any personal property taxes). Language was included in the House that any revenue loss to local governments would be reimbursed by the State. However, these monies would require an appropriation by the Legislature.

Property Assessment Cap

Proposal A limits the growth in taxable value to the lesser of inflation or 5 percent. The inflation factor for this calculation is published by the State Tax Commission and is:

2004	2.3%
2003	1.5%
2002	3.2%
2001	3.2%
2000	1.9%
1999	1.6%
1998	2.7%
1997	2.8%
1996	2.8%
1995	2.6%
1994	3.0%

The 2003 inflation factor was used for property taxes levied in the City’s fiscal year ended June 30, 2004. Property taxes are the City’s largest source of General Fund revenue. However, as indicated above, growth in existing property can be significantly limited due to Proposal A. This factor should be considered when the City is performing long-term financial planning.

Also, as you probably recall, the Headlee Amendment to the Michigan Constitution limits the amount of taxes that can be levied by the City. In general terms, if growth on the City’s existing property tax base exceeds inflation for a particular year, the Headlee Amendment requires the City to “roll back” its property tax rate to inflation. Prior to the passage of Proposal A in 1994, during years when the growth on the City’s existing property tax base was less than inflation, the Headlee Amendment allowed the City to “roll up” its property tax rate and recover from years when the property tax rate was “rolled back”. However, subsequent to the passage of Proposal A and as a result of changes made to the State’s General Property Tax Act, the City is no longer allowed to “roll up” its property tax rate in years when growth on its existing tax base is less than inflation.

For the year ended June 30, 2004, the City’s Headlee maximum property tax rate for its operating levy was 18.6847 mills even though City Charter would allow the City to levy 20.0 mills for operations. Because of changes made to the General Property Tax Act in 1994, this reduction in millage rate is permanent absent a Headlee override vote. Additionally, as demonstrated by a recent study published by the Michigan Municipal League (with the

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participation of the Michigan Townships Association and the Michigan Association of Counties), due to definitional changes made to the General Property Tax Act in 1994, the treatment of uncapped values or the "pop up" amount when a property is transferred or sold (as growth on existing property subject to the Headlee rollback calculation), the downward pressure on millage rates will continue particularly given the significant gap that now exists between taxable value and state equalized value.

HEALTH CARE COSTS

Prescription Drug Program

It is our understanding that the State of Michigan may be offering local governments the opportunity to participate in the State's prescription drug program. A presentation was made in September 2004 to introduce this program to local governments. While we have not evaluated the program, the City may want to consider this option as it evaluates and continues to try to control its health care costs.

Retiree Health Care Costs

The Governmental Accounting Standards Board has recently released Statement Number 45, Accounting and Reporting by Employers for Postemployment Benefits Other Than Pensions. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree health care, as well as any "other" postemployment benefits (other than pensions). The new rules will cause the government wide financial statements to recognize the cost of providing retiree health care coverage over the working life of the employee, rather than at the time the health care premiums are paid. The new pronouncement is effective for the year ended June 30, 2010.

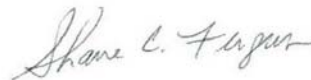
We would like to thank you and your staff again this year for their cooperation and assistance provided during the audit. If you have any questions, or would like to discuss these items further, please feel free to contact us at your convenience.

Yours truly,

PLANTE & MORAN, PLLC



Michael J. Swartz



Shane C. Ferguson